

## EQUITIES PERSPECTIVE

April 3, 2009  
DJIA: 7,978

Now you see them . . . now you don't. From "mark-to-market" to mark-to, well, whatever, and away with those nasty write downs. With a Congressional gun to their head the board that sets accounting rules in the US will change the rule that has forced banks to report growing losses as the values of their mortgage backed securities have crumbled. As you've no doubt heard, the change is not without controversy. After all, wouldn't we all like the opportunity to value our portfolios at what we "think" they're worth. The change, surprise, is generally supported by the Banks. Banks argue that current market values are unreasonably low, reflecting distressed trading that produces values well below the amount that ultimately will be realized. And they have a point. A distressed bank's sale of a million dollars of distressed securities shouldn't affect a billion dollars of securities in a non-distressed bank. Then, too, we all know the only real measure of what something is worth is what you can sell it for. And while no doubt there are securities that are undervalued, we've also noticed in general the toxic paper isn't exactly getting better. But hey, as long as the market likes it.

These days, of course, there seems little the market doesn't like. Even the likely GM bankruptcy was only good for a day or two of decline. Then, too, these days a bad day like Monday can be like a week in terms of Dow points. But the Friday-Monday weakness, which almost seemed overdue, was surprisingly well contained. Though above Friday's, Monday's NY volume wasn't great, but NASDAQ volume contracted. With the NASDAQ seemingly leading here, volume there expanded Tuesday, Wednesday and Thursday. Wednesday's down-to-up reversal also was impressive, and Thursday's modest fade at the close didn't detract from another good day. Whether a new bull market or a bear market rally, markets don't go straight up. But momentum like this doesn't just turn and go away. As long as corrections keep looking like Friday-Monday, that's fine. And as long as the subsequent rallies look like Tues-Thurs, especially in terms of volume, that's even better.

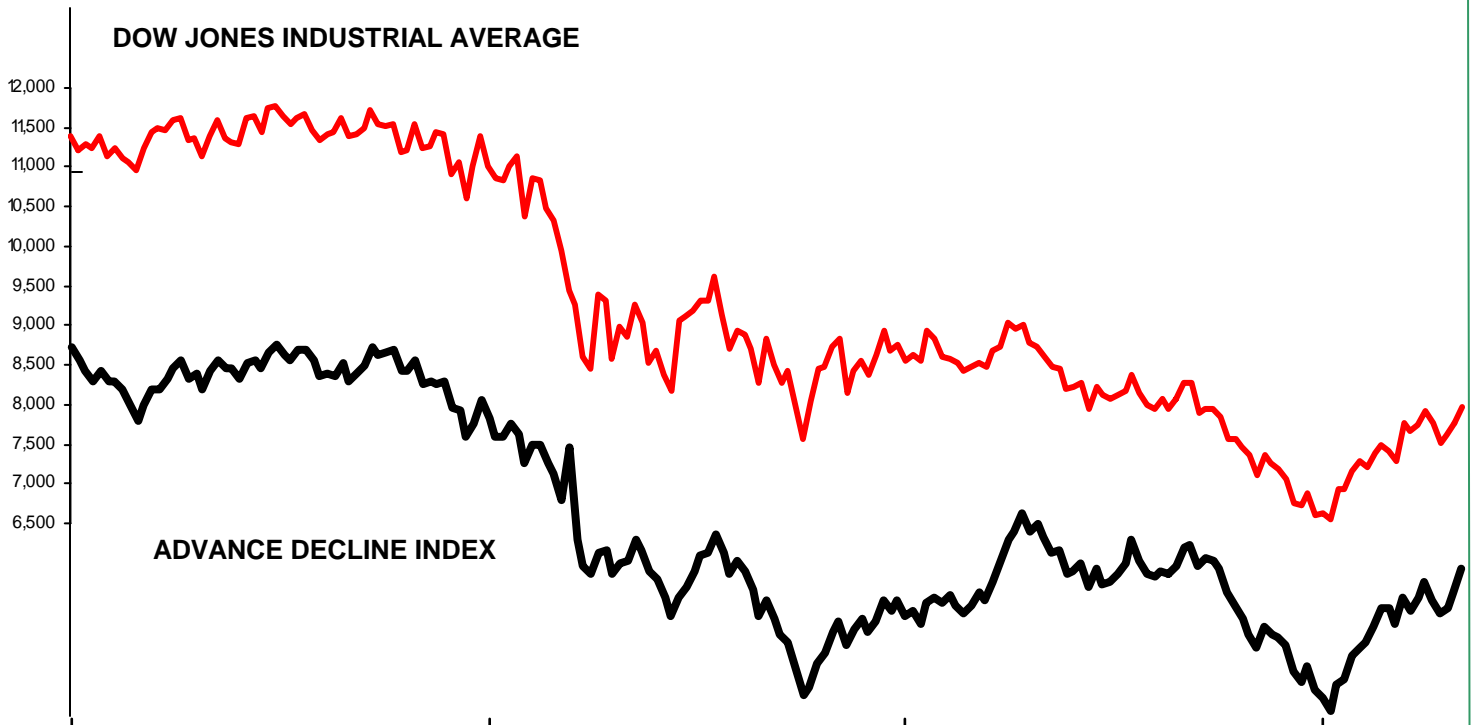
For most of us, market volatility still seems the rule. Yet, based on the VIX or Volatility Index, volatility is quite subdued when compared to last fall. Last year the global financial crisis and resulting panic selloff caused a record rise in volatility as measured by the VIX. Some might argue that the failure of the VIX to rise in early March, as is typical at market lows, suggests this is yet another oversold rally such as we've seen several times in the past year. However, not only is it possible, it seems likely that the March low was just different. While last fall marked the panic low – record volume and new lows – like November, March was another low in a bottoming process. Over the past decade there has been a close correlation between market volatility and the direction of the equities market. In that sense, the ability for market volatility to remain stable this year, despite lower lows in the market, seems a positive sign, a positive divergence. The decline in volatility could be a sign that economic visibility is increasing, as is investor's tolerance for risk.

Another difference in this recovery has been what's leading. At a low, down the most typically rallies the most. After dragging the market down into early March, Financials have rebounded to become the strongest sector. While typical for now, that's likely to be short lived. Meanwhile, areas like Retail, Semi's and Tech generally, didn't suffer as did the Financials and, in fact, suffered relatively little compared to their declines into the November low. Looking at the charts, one can easily argue that for these groups March was a test of the November lows, and the period since then has been part of a bottoming process. And, a bottoming process here argues for a bottoming process for the market. Bear market rallies rally everything, as per the rally in Financials. But the look of Retail and the Semi's is not what you would expect in a typical bear market rally. In a bear market not everything reaches its low at the same time, and those that hold up best tend to lead.

Bank of America (7.3), should've bought it back at \$2.50. And those houses, maybe we should be buying then before it's too late. There's nothing like higher prices to make things look better. Suddenly the Banks will be okay and profitable again. There are signs of healing. We're not sure where this came from, but now they tell you a 20% rally is the definition of a new bull market. It's as though they don't believe, but they're not sure – is this the real thing, they ask. If by real thing you mean a good rally, of course it's the real thing. Doubtful it's a new bull market, but who cares? It's a good rally, the market is going higher. Sure there will be corrections, there are corrections in bull markets and bear market rallies, that doesn't tell you which this might be. Whether bull or bear there seems more to go, corrections aside. It seems likely, in fact, you don't really start worrying until most start believing.

Frank D. Gretz

# STOCK AVERAGE VS. AVERAGE STOCK



Jul-01-08

Nov-13-08

Apr-02-09

